

Message Text

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ORIGIN SS-25

INFO OCT-01 ISO-00 SSO-00 CCO-00 INRE-00 /026 R

DRAFTED BY: EB/ICD:WAVEINGARTEN:MBL
APPROVED BY: EB:JAGREENWALD
EB/ORF/ICD:EAWENDT
EB/ORF:SWBOSWORTH
E:JEINHORN
S/S:O - LRMACFARLANE

----- 126706

O 040010Z AUG 76
FM SECSTATE WASHDC
TO AMEMBASSY LONDON IMMEDIATE
AMEMBASSY CANBERRA IMMEDIATE
AMEMBASSY BRASILIA IMMEDIATE
INFO AMCONSUL RIO DE JANEIRO IMMEDIATE

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STADIS/////////
EXDIS TODEP 39

C O R R E C T E D C O P Y (TODEP 39 ADDED TO CAPTION LINE)

E.O. 11652: N/A

TAGS: EFIN

SUBJECT: INTERNATIONAL RESOURCES BANK: UNRESOLVED ISSUES

FOR ROBINSON AND ROGERS FROM GREENWALD
FOR BRASILIA: PLEASE PASS CHARLES FRANK

1. IN CLEARING THE IRB QUESTIONS AND ANSWERS PAPER WITH
TREASURY, WE WERE UNABLE TO REACH AGREEMENT ON TWO ISSUES:
(A) THE EXTENT TO WHICH THE IRB SHOULD ACT AS A RESIDUAL
GUARANTOR FOR HOST GOVERNMENT OBLIGATIONS TO PRIVATE
LENDERS; AND (B) WHETHER THE IRB SHOULD HAVE AUTHORITY
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TO RAISE FUNDS FOR SPECIFIC PROJECTS BY ISSUING BONDS
IN ITS OWN NAME, BACKED BY ITS GENERAL CREDIT. BOTH OF
THESE ARE KEY ISSUES AND MUST BE ADDRESSED IN ANY MEANING-
FUL ELABORATION OF OUR PROPOSAL SUCH AS IN THE QUESTIONS

AND ANSWERS.

2. FOLLOWING IDENTIFICATION OF THESE ISSUES, WE PREPARED AN ISSUES PAPER FOR PRESENTATION TO THE COMMODITIES POLICY COORDINATING COMMITTEE(CPCC), WHICH MET AUGUST 2. ANALYSIS AND PROS/CONS OF EACH ISSUE FOLLOW AS PRESENTED TO CPCC.

3. ISSUE ONE: EXTENT TO WHICH THE IRB SHOULD ACT AS A RESIDUAL GUARANTOR FOR HOST GOVERNMENT OBLIGATIONS TO PRIVATE LENDERS.

ANALYSIS: IN ANY INVESTMENT PROJECT, PRIVATE NON-EQUITY LENDERS (COMMERCIAL BANKS, ETC.) INSIST ON VARIOUS GUARANTEES AS CONDITIONS TO THEIR LOANS. THESE WOULD INCLUDE GUARANTEES ON SUCH SPECIFIC, NON-COMMERCIAL QUESTIONS AS REPATRIATION OF PROFITS, FOREIGN EXCHANGE CONVERTIBILITY, ETC. A BANK WILL ALSO INSIST UPON GUARANTEES, EITHER FROM THE HOST GOVERNMENT OR PRIVATE EQUITY INVESTOR OR BOTH, FOR REPAYMENT OF LOANS, REDEMPTION OF BONDS, ETC. IN THE EVENT OF THE COMMERCIAL FAILURE OF THE PROJECT. IN OTHER WORDS, WHILE THE BANKS TRY TO SATISFY THEMSELVES AS TO THE COMMERCIAL VIABILITY OF ANY GIVEN PROJECT, THEY WILL ALSO SATISFY THEMSELVES AS TO THE CREDIT WORTHINESS OF THE BORROWER, I.E. ABILITY TO REPAY IN THE EVENT THE PROJECT GOES BUST, BEFORE LENDING MONEY.

IT IS AGREED THAT THROUGH ITS PARTICIPATION IN THE TRI-LATERAL AGREEMENT, THE IRB WOULD ACT AS A RESIDUAL GUARANTOR FOR THE FIRST TYPE OF RISK,WHICH WOULD PRESUMABLY BE SPECIFIED IN THE AGREEMENT. THUS, IF THE LOANS WERE NOT REPAYED OR THE BONDS NOT REDEEMED BECAUSE THE HOST GOVERNMENT RENEGED ON ITS COMMITMENTS CONCERNING PROFIT REPATRIATION, ETC., THE IRB WOULD STEP IN AND PAY OFF THE PRIVATE LENDER AND THEN PURSUE THE HOST GOVERNMENT FOR REPAYMENT THROUGH WHATEVER PROCEDURES MIGHT BE ESTABLISHED.

HOWEVER, IT IS NOT AGREED WHETHER THE IRB SHOULD ACT AS LIMITED OFFICIAL USE
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A FULL RESIDUAL GUARANTOR, STANDING BEHIND THE HOST GOVERNMENT'S REPAYMENT OBLIGATIONS, SHOULD THE HOST GOVERNMENT RENEGE FOR WHATEVER REASON. THIS TYPE OF GUARANTEE WOULD MEAN THAT IF A GIVEN PROJECT COLLAPSED FOR WHATEVER REASON (E.G., INACCURATE PROJECTIONS OF DEVELOPMENT COST, DECLINE IN WORLD PRICE FOR THE PRODUCT, ETC.), AND THE HOST GOVERNMENT WAS UNWILLING OR UNABLE TO REPAY THE PRIVATE LENDER, THE IRB WOULD BE OBLIGATED TO PAY THE LENDER.

PROS:

-- AS A FULL RESIDUAL GUARANTOR THE IRB WOULD BE CONSIDERABLY MORE ATTRACTIVE TO INVESTORS.

-- THE IRB, AS FULL RESIDUAL GUARANTOR, WOULD ATTRACT MORE FINANCIAL INSTITUTIONS TO LEND TO RESOURCE DEVELOPMENT IN DEVELOPING COUNTRIES.

CONS:

-- IT WOULD INEVITABLY REQUIRE THAT THE IRB TAKE ON ON THE RESPONSIBILITY NOW ASSUMED BY THE PRIVATE LENDERS OF ASSURING ITSELF OF (1) THE COMMERCIAL VIABILITY OF A GIVEN PROJECT; AND (2) THE CREDIT WORTHINESS OF A GIVEN BORROWER, THUS REQUIRING A CONSIDERABLY LARGER IRB STAFF.

-- THIS WOULD INCREASE CONSIDERABLY IRB EXPOSURE.

4. ISSUE TWO: SHOULD THE IRB HAVE AUTHORITY TO RAISE FUNDS FOR SPECIFIC PROJECTS BY ISSUING BONDS IN ITS OWN NAME BACKED BY ITS GENERAL CREDIT?

RATHER THAN ACTING SIMPLY AS A SALES AGENT, THE IRB WOULD ISSUE BONDS IN ITS OWN NAME, RELENDING THE PROCEEDS TO THE PROJECT PARTICIPANTS. (THESE COULD BE SUPPLEMENTAL TO BONDS ISSUED BY THE PROJECT IN WHICH THE IRB'S LIABILITY WOULD BE LIMITED TO SPECIFIED NON-COMMERCIAL RISK.) THE IRB COULD THUS TAP A BROAD SPECTRUM OF PRIVATE FINANCIAL MARKETS FOR CAPITAL FOR RELENDING TO RESOURCE

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DEVELOPMENT PROJECTS. A SUBSIDIARY ISSUE IS WHETHER THE IRB COULD ACT AS A TRUE UNDERWRITER FOR BONDS ISSUED BY THE PROJECT THUS EXPOSING ITSELF TO HOLDING BONDS WHICH IT DOES NOT SELL AND WHICH IT PAYS FOR FROM ITS OWN RESOURCES. PRESUMABLY AS LENDER OR HOLDER OF PROJECT BONDS, THE IRB WOULD INSIST ON A HOST COUNTRY GOVERNMENT GUARANTEE AS DOES THE IBRD.

PROS:

-- HAVING THIS AUTHORITY WOULD MAKE THE IRB CONSIDERABLY MORE ATTRACTIVE TO THE LEC'S AS A MOBILIZER OF INCREMENTAL CAPITAL.

-- THIS WOULD INCREASE SUBSTANTIALLY IRB FLEXIBILITY IN SELECTING AND ANALYZING SPECIFIC RESOURCE DEVELOPMENT PROJECTS.

-- THIS CAPABILITY WOULD DISTINGUISH THE IRB FROM A STRAIGHT MULTILATERAL INSURANCE FACILITY.

-- IF THE IRB IS PROVIDING ITS OWN RESOURCES, ITS
NEGOTIATING POSITION WITH RESPECT TO THE TRILATERAL

AGREEMENT WOULD BE CONSIDERABLY STRENGTHENED.

CONS:

-- THIS WOULD GREATLY INCREASE IRB EXPOSURE AS IT WOULD
BE LIABLE FOR COMMERCIAL AS WELL AS POLITICAL RISK AND
WOULD REQUIRE A SUBSTANTIALLY LARGER CAPITALIZATION THAN
IS NOW FORESEEN.

-- THE IRB WOULD BE AN ADDITIONAL CLAIMANT ON THE US
CAPITAL MARKET.

-- THE IRB WOULD BE DUPLICATING SOME OF THE FUNCTIONS
NOW PERFORMED BY THE IBRD.

5# IN PRELIMINARY CPCC DISCUSSION ON AUGUST 2 ALL OTHER
AGENCIES TOOK THE POSITION THAT IT WOULD BE CONTRARY TO
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BASIC INTERAGENCY DECISIONS ON THE IRB PROPOSAL TO GIVE IT
THE CAPAB-
ILITY EITHER TO ACT AS FULL RESIDUAL GUARANTOR
OR TO ISSUE BONDS IN ITS OWN NAME. THEY ARGUE THAT GIVING
THE IRB EITHER CAPABILITY WOULD REQUIRE SUBSTANTIAL EXPAN-
SION OF CAPITAL BASE AND WOULD TAKE IRB I TO ACTIVITIES
BETTER LEFT TO THE PRIVATE SECTOR. I WOULD APPRECIATE
YOUR VIEWS BEFORE THE NEXT CPCC MEETING ON AUGUST 6 AS
TO WHETHER WE SHOULD KEEP ONE OR BOTH OF THESE ISSUES OPEN
IN THE CURRENT CPCC REVIEW OF THE Q'S AND A'S. IF WE DO,
WE WOULD THEN HAVE TO PRESENT THEM PROMPTLY TO THE EPB
FOR DECISION.
ON BALANCE, WHILE I AGREE THAT THE CAPABILITY TO ACT AS
FULL RESIDUAL GUARANTOR AND THE AUTHORITY TO ISSUE BONDS
IN ITS OWN NAME WOULD MAKE THE IRB SOMEWHAT MORE ATTRACTIVE
TO BOTH LDCS AND PRIVATE LENDERS, I DO NOT BELIEVE EITHER
CAPABILITY IS NECESSARY TO MEET THE OBJECTIVES FOR WHICH
THE IRB IS DESIGNED. ALSO, IT IS VERY CLEAR THAT ANY
EFFORT TO GIVE IT SUCH AUTHORITY NOW WOULD BRING ON THE
FULL OPPOSITION OF TREASURY, OMB, CEA AND OTHERS.
IF EITHER OF THESE ISSUES ARISES AS A MAJOR OBSTACLE TO
OBTAINING NECESSARY SUPPORT FOR IRB DURING ACTUAL
NEGOTIATIONS, WE COULD THEN REOPEN THE QUESTION WITHIN THE
USG.

6. THE CPCC ALSO DISCUSSED OUR DRAFT OPTIONS PAPER ON THE
UNCTAD COMMON FUND. INTERAGENCY
THINKING IS MOVING TOWARD THE MIDDLE GROUND BETWEEN

SIMPLE ACCEPTANCE OF THE UNCTAD SCHEME AND OUTRIGHT
OPPOSITION. THE POSSIBILITIES WILL INCLUDE SOME VERSITN
OF THE FRENCH PROPOSAL FOR FINANCIAL LINKAGE AMONG BUFFER
STOCK FUNDS ONCE THEY ARE AGREED AS WELL AS PARTICIPATION
I THE NEGOTIATIONS ON THE IOMMON FUND WITH THE OBJECTIVE
OF TURNING IT INTO SOMETHING WE COULD LIVE WITH. A
REVISED VERSION OF OUR PAPER IS SCHEDULED TO GO TO THE
EPB TOWARD THE END OF AUGUST. KISSINGER

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Message Attributes

Automatic Decaptioning: Z
Capture Date: 15 SEP 1999
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: AGREEMENT DRAFT, BANKS
Control Number: n/a
Copy: SINGLE
Draft Date: 04 AUG 1976
Decaption Date: 28 MAY 2004
Decaption Note: 25 YEAR REVIEW
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: coburnhl
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1976STATE192459
Document Source: ADS
Document Unique ID: 00
Drafter: EB/ICD:WAWERINGARTEN:MBL
Enclosure: n/a
Executive Order: N/A
Errors: n/a
Film Number: D760299-0617
From: STATE
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1976/newtext/t197608103/baaaepz.tel
Line Count: 227
Locator: TEXT ON-LINE, TEXT ON MICROFILM
Office: ORIGIN SS
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: EXDIS
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 5
Previous Channel Indicators:
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: EXDIS
Reference: n/a
Review Action: RELEASED, APPROVED
Review Authority: coburnhl
Review Comment: n/a
Review Content Flags:
Review Date: 19 MAY 2004
Review Event:
Review Exemptions: n/a
Review History: RELEASED <19 MAY 2004 by buchant0>; APPROVED <08 SEP 2004 by coburnhl>
Review Markings:

Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
04 MAY 2006

Review Media Identifier:
Review Referrals: n/a
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
Secure: OPEN
Status: NATIVE
Subject: INTERNATIONAL RESOURCES BANK: UNRESOLVED ISSUES
TAGS: EFIN, XX, UK
To: LONDON
CANBERRA
BRASILIA INFO RIO DE JANEIRO
Type: TE
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 04 MAY 2006